Inclusionary Housing Working Group: Final Recommendations

Office of the Controller

February 1st 2017

Outline

- Review of Prior Recommendations
- Phase 2 Findings and Conclusions
- Proposed State Density Bonus Approach
- Final Recommendations
  - Base Project Requirements Including Fee Alternative
  - Density Bonus Approach

Review of Phase 1 Recommendations

1. Separate requirements for ownership and rental projects
2. On-site requirements:
   - 17-20% - Ownership
   - 14-18% - Rental
3. 0.5% annual increases in on-site requirements for both ownership and rental projects
4. Separate process for 80/20 Projects
5. Phase 2 Work
   1. Density Bonus
   2. Income limit sensitivity analysis
   3. Fee equivalence to recommended on-site requirements
   4. When should affordable housing requirements vest?

Phase 2 Findings and Conclusions

- Income limits sensitivity: Changing the income limits from 60/40 low/medium income to a minimum of 12% low-income, with remainder middle income, changes the on-site feasibility thresholds only slightly. Our report will note the ranges but make no recommendations about appropriate income limits.
- Equivalent Fees: 18-23% for Rental, 25-28% for Ownership, based on MOHCD's 2016 fees.
- When should requirements apply? We have decided not to include this question in the study as it is a policy issue not directly related to feasibility.
- Density Bonus Proposal – discussed on the next page

Density Bonus Proposal

- While local governments may not require on-site affordable units on the bonus units, impact fees for infrastructure and City services may be charged.
- San Francisco's inclusionary housing requirement takes the form of impact fee, which may be met through the provision of on-site (or off-site) units, in lieu of paying the fee.
- As there is no reason to believe that bonus units have any different impact on affordable housing needs than base units, the City could require the same fee be paid on the bonus units.
- If the City adopted this approach, developers would have the option of meeting their inclusionary requirement with enough on-site units to be eligible for a density bonus, while paying the impact fee for the bonus units.
- This approach has the advantage of increasing the inclusionary housing contribution of projects that elect to take the density bonus, while not harming the feasibility of projects that do not.
- An illustration of how the requirement currently works, and would work under this proposal, is shown on the next three pages.

Inclusionary Housing Options: An Example of How it Works Now, Assuming No Density Bonus

- Project Assumptions:
- 100 condo units (30 studio, 40 1 bedroom, 30 2 bedrooms)
- 17% on-site requirement, 25% fee percentage
- Requirements are within the feasible range determined in Phase 1
- 2016 MOHCD fees apply

Option 1: On-Site
83 units of Market-rate
17 units of BMR
$0 fee payment

Option 2: Fee
100 units of Market-rate
0 units of BMR
fee payment: 25% x 30 x $198,008 + 25% x 40 x $268,960 + 25% x 30 x $366,369 $6,922,428

Current Options for the Same Project With 35 Bonus Units (10 Studios, 15 1BRs, 10 2BRs)

- If the project takes the density bonus, currently its inclusionary requirements do not change.

Option 1: On-Site
118 units of Market-rate (83 base + 35 bonus)
17 units of BMR
$0 fee payment

Option 2: Fee
Not eligible for density bonus

The Proposed Approach Would Apply to All Density Bonus Projects

- Projects electing the density bonus would pay a fee on the bonus unit, and build on-site in lieu of a fee to qualify for the density bonus. as shown below as Option 3.
- Developers currently have the option to meet their requirements through a combination of on-site units and fee payments, so this would not be a new policy.

Option 1: On-Site, No Density Bonus
83 units of Market-rate
17 units of BMR
$0 fee payment

Option 2: Fee, No Density Bonus
100 units of Market-rate
0 units of BMR
fee payment: 25% x 30 x $198,008 + 25% x 40 x $268,960 + 25% x 30 x $366,369 $6,922,428

Option 3: Onsite + Fee With Density Bonus
118 units of Market-rate (83 base + 35 bonus)
17 units of BMR
fee payment: 25% x 10 x $198,008 + 25% x 15 x $268,960 + 25% x 10 x $366,369 $2,419,543

Value Capture Associated with the Proposal

- Research from the Consulting Team suggests bonus units would be feasible at a higher fee than base units. However, there is no legal basis for charging a different impact fee on bonus units than is charged on base units. so we are recommending a single fee percentage that would apply to all units.
- The proposed approach would lead to a fee payment, for our sample project, equal to approximately 80% of what would have been charged if the maximum feasible fee was charged on bonus units.
- Because the same fee must be charged on all units, charging a higher fee in order to recapture additional value from bonus units would have the effect of making certain projects that do not take the density bonus infeasible, thereby reducing both market rate and BMR housing production.
- If, in the future, almost all projects take the density bonus, it might make sense to raise the single fee charged on all projects to capture more of the value. The Controller's Office plans to study this as part of its next 3-year review of the policy.

Additional Recommendations for TAC Action

1. Should the City set the Fee Option at 18-23% for Rental, 25-28% for Ownership to maintain equivalence with previous on-site recommendations?
2. Should the City apply the fee to all units in a project, for density bonus and non-density bonus projects?
3. Should the Controller and TAC reconvene in 3 years to reconsider feasibility, density bonus, and other issues, and produce an updated report?